

## TAX RELEASES

*("Tax Releases" are designed to provide answers to the specific tax questions covered, based on the facts indicated. However, the answer may not apply to all questions of a similar nature. In situations where the facts vary from those given herein, it is recommended that advice be sought from the Department. Unless otherwise indicated, Tax Releases apply for all periods open to adjustment. All references to section numbers are to the Wisconsin Statutes unless otherwise noted.)*

## INCOME TAXES

### I. Federal Revenue Rulings Issued In 1980

**Facts and Question:** Do 1980 federal revenue rulings affect Wisconsin? For the 1980 taxable year, Wisconsin follows the federal law in effect as of December 31, 1979 in computing income and deductions, with exceptions for special federal provisions for benefits received from an employer's educational assistance program, foreign living cost deductions, and amortization of pollution control facilities. Federal laws enacted in 1980 do not apply for Wisconsin for 1980. A question has been raised whether a federal revenue ruling issued in 1980 applies to Wisconsin for the taxable year 1980.

**Answer:** A federal revenue ruling is an Internal Revenue Service interpretation of an existing federal law. If a federal revenue ruling issued in 1980 or thereafter relates to an interpretation of a federal law enacted on or before December 31, 1979, the revenue ruling will apply for Wisconsin as well as federal for the taxable year 1980. For example, Revenue Ruling 80-275, which was issued in 1980 (as indicated by the first two serial numbers of the ruling), applies to Wisconsin for 1980, since it interprets a law which was enacted on or before December 31, 1979.

If a revenue ruling was issued in 1980 which interpreted a federal law enacted after December 31, 1979, such revenue ruling would not apply to Wisconsin for 1980 because for the taxable year 1980, Wisconsin does not follow federal laws (or interpretations thereof) which were enacted after December 31, 1979.

### II. 12% Rent Credit/Homestead Credit Based on Rent Paid by the Performance of Services

**Facts & Questions:** Situation #1 - A resident manager occupies an apartment for which the normal rent is \$3,600 per year. Because of her managerial services she is only required to pay \$1,200.

Situation #2 - A resident manager occupies an apartment free of charge. The normal rent is \$4,800. As manager, he is paid \$5,000 cash for performing managerial services. The entire \$9,800 (\$4,800 + \$5,000) is subject to social security tax, but only \$5,000 is subject to income tax.

Situation #3 - A minister employed as a teacher at a parochial school receives a rental allowance of \$1,200 per year from the church and this rental allowance is determined to be not includible in income for tax purposes. He makes total cash rental payments of \$2,400 per year to his landlord.

Situation #4 - A minister of a church occupies a parsonage rent free. The parsonage is assessed real property

taxes of \$1,000 which the church pays. The fair rental value of the house is \$4,200 per year.

What amount of rent may be used to compute the rent credit under s. 71.53 and homestead credit under 71.09(7) assuming the persons in these 4 situations qualify for these credits.

**Answers:** Situation #1: For both the 12% rent credit and homestead credit, the manager may use total rent of \$3,600 (\$1,200 in cash and \$2,400). The fair rental value of services performed, as measured by the \$2,400 reduction in rent allowed, constitutes rent paid in cash or its equivalent.

Situation #2: The manager may base his 12% rent credit and homestead credit on \$4,800 of tax free rent, which is deemed to be rent paid by equivalent services.

Situation #3: The minister employed as a teacher is able to claim both the 12% rent credit and homestead credit based on rent paid of \$2,400, even though \$1,200 of the teacher's salary designated for housing is not includible in taxable income.

Situation #4: The minister is considered to have paid rent in the form of ministerial services for the free rent received. The 12% rent credit and homestead credit are based on the total fair rental value of the residence of \$4,200. Fair rental value means the rent that would normally be paid at arms length. If the parsonage was exempt from real property tax, no rent credit or homestead credit would be allowed unless the exempt housing is owned and operated by a public housing authority, which makes payments in lieu of property taxes to the municipality in which the property is located.

In all of the above situations, rent paid in cash or its equivalent must be reduced as follows: For the 12% rent credit, rent paid must be reduced by the reasonable value of domestic, food, medical or other services furnished by the landlord which are unrelated to use of the dwelling as housing. For homestead credit, rent must be reduced by the reasonable value of utilities, and the reasonable fair rental value of furniture and appliances furnished by the landlord.

Limitations are applied to the amount of rent used in the computations. For the rent credit, 20% of the rent is considered if the landlord furnishes the heat, or 25% if the tenant furnishes the heat. For homestead credit, 25% of the rent for occupancy only is considered, limited to \$1,000 for the year 1980.

### III. 12% Rent Credit-Computing Rent Paid By Farmers Operating on Shares

**Facts & Question:** Many agreements between operating farmers and landowners state that each will provide certain property, supplies or services, and gross receipts will be split between them in some manner. For example, assume the agreement provided for the farmer to live in a house owned by the landowner and for the farmer to give 25% of the crop proceeds to the landowner. For 1979, the landowner received \$2,000 from the farmer as the landowner's 25% share of the crop proceeds. In this example, how is the farmer's "rent paid" computed for purposes of determining the 12% rent credit under s. 71.53, Wis. Stats.?

**Answer:** The amount which may be used as "rent paid" by such farmers for the 12% rent credit allowed on 1979 and subsequent years Wisconsin individual income tax returns is the fair rental value of the residence. For example, if the fair rental value of the residence was \$1,200, the amount of "rent paid" for the 12% rent credit would be \$1,200. However, if the fair rental value of the residence was \$2,400, the "rent paid" could be no more than the total crop proceeds paid to the landowner, i.e., \$2,000 in this example.

The fair rental value of the residence should be determined by comparing the cost of renting similar residences in the area. The fair rental value can be established by obtaining an appraisal from a qualified real estate or rental agent, or by a reasonable determination made by the landowner. The fair rental value may be questioned by the department if the amount appears unreasonable.

#### IV. Itemized Deduction For Death Taxes

**Facts and Question:** Under Internal Revenue Code section 691(c), a miscellaneous itemized deduction is allowed for federal estate taxes (reduced by any credits against the tax) attributable to income in respect of a decedent.

Effective for the 1979 taxable year and thereafter, s. 71.02(2)(f), Wis. Stats., excludes itemized deductions for taxes allowable under section 164 of the Internal Revenue Code. Section 164 of the Code provides for a deduction of state and local income taxes, real estate taxes, gas taxes, sales taxes, and personal property taxes.

Can individuals claim federal estate taxes attributable to income in respect of a decedent as an itemized deduction for Wisconsin purposes in the 1979 taxable year and subsequent taxable years?

**Answer:** Yes, since Wisconsin law excludes only deductions for taxes allowable under section 164 of the Internal Revenue Code, the deduction for death taxes provided under section 691(c) continues to be available for Wisconsin purposes in 1979 and subsequent years as a miscellaneous itemized deduction.

#### V. How to Prorate Deductions and Personal Exemption Credits When Husband and Wife Have Different Residency Status

##### BACKGROUND:

Part-year residents and nonresidents of Wisconsin are required to prorate their itemized deductions or standard deduction and personal exemption credits on their Wisconsin income tax returns. For married persons (both nonresidents and part-year residents), the proration of itemized deductions or the standard deduction is based on the ratio of their combined Wisconsin total income to their joint or combined federal adjusted gross income. (Section 71.02(2)(f) for itemized deductions and Section 71.02(2)(gq)7 for the standard deduction.) The proration of personal exemption credits for nonresidents is based on this same ratio (Section 71.09(6p)(d)2). The proration of personal exemption credits for part-year residents is based on the number of months they were Wisconsin residents (Section 71.09(6p)(d)1).

The question arises as to how the deductions and personal exemption credits should be computed where resi-

dency status of one spouse is different than the residency status of the other spouse.

##### LAW RELATING TO PRORATION:

Section 71.02(2)(f) - Itemized Deductions "Itemized deductions means deductions from federal adjusted gross income allowable under the internal revenue code in determining federal taxable income, other than the federal standard deduction, low-income allowance and deductions for personal exemptions; but with respect to nonresident natural persons deriving income from property located, business transacted or personal or professional services performed in this state, including natural persons changing their domicile into or from this state in the calendar year 1972 or corresponding fiscal year or thereafter, "itemized deductions" are limited to such fraction of the amount so determined as Wisconsin adjusted gross income is of federal adjusted gross income, except for married persons "itemized deductions" are limited to such fraction of the amount so determined as combined Wisconsin adjusted gross income is of combined or joint federal adjusted gross income."

Section 71.02(2)(gq)7 - Standard Deduction "With respect to nonresident natural persons deriving income from property located, business transacted or personal or professional services performed in this state, including natural persons changing their domicile into or from this state, for the taxable year 1977 and thereafter, the low-income allowance authorized under this paragraph is limited by such fraction of that amount as Wisconsin adjusted gross income is of federal adjusted gross income for unmarried persons, and as combined Wisconsin adjusted gross income is of combined or joint federal adjusted gross income for married persons."

Section 71.09(6p)(d) - Personal Exemption Credits "Beginning with the calendar year 1975 and corresponding fiscal years and thereafter, the deduction for personal exemptions provided for in this subsection shall be limited as follows:

1. With respect to persons who change their domicile into or from this state during the taxable year, personal exemptions shall be limited to such fraction of the amount so determined that the time of domicile within this state is of the total time during the taxable year, but the total deduction for all personal exemptions shall not be less than \$5.

2. With respect to nonresident persons, personal exemptions shall be limited to such fraction of the amount so determined as Wisconsin adjusted gross income is of federal adjusted gross income, except that for married persons personal exemptions shall be limited to such fraction of the amount so determined as combined Wisconsin adjusted gross income is of combined federal adjusted gross income, but the total deduction for all personal exemptions shall not be less than \$5."

HOW TO DETERMINE PRORATION

When husband and wife have different periods of Wisconsin residency, the spouse who claims the deduction or exemptions determines what, if any, proration must be made. This means that a different total deduction or exemption credit may be allowable on a tax return, depending on which spouse actually claims the deductions or the exemption credit. The following examples indicate how the itemized deductions, standard deduction and personal exemption credits are prorated when husband and wife have different periods of Wisconsin residency during a taxable year:

Part-year residents prorating personal exemption credits must use the following proration ratios:

Number of Months a Resident	Proration Ratio	Number of Months a Resident	Proration Ratio
1 month	= .083	7 months	= .583
2 months	= .167	8 months	= .667
3 months	= .250	9 months	= .750
4 months	= .333	10 months	= .833
5 months	= .417	11 months	= .917
6 months	= .500	12 months	= 1.00

EXAMPLES:Situation 1: Full-year resident and part-year residentFACTS:

Taxpayer is a full-year Wisconsin resident who marries a person who is a nonresident until marriage in 1980. His wife then becomes a Wisconsin resident. She is a Wisconsin resident for six months in 1980.

Joint federal adjusted gross income (husband & wife)	\$20,000
Husband's Wisconsin total income (1980 Form 1, Line 38)	\$13,000
Wife's Wisconsin total income (1980 Form 1, Line 38)	\$ 2,000
Total itemized deductions available for Wisconsin	\$ 4,000

SOLUTION:

Any portion of the itemized deductions claimed by the husband (a full-year resident) are not prorated. If he claims the full \$4,000, the entire amount is allowable. If the wife would claim any portion of the itemized deductions, that portion would be prorated in a ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income. For example, if the husband claims \$3,000 of the itemized deductions, that amount would not need proration. The other \$1,000 allocated to the wife (a part-year resident) would be prorated using a proration percentage of 75% [ $15,000$  (Wis. Total Income of H & W)  $\div$   $20,000$  (Fed. Adj. Gross Income of H & W) = 75%]. She would be allowed a deduction of \$750 ( $\$1,000 \times 75\%$ ). The same reasoning would be used in determining how much personal exemption credit would be allowed. There are two exemptions (\$20 for each spouse) for a total of \$40. If the husband claimed the full \$40, there would be no proration. If the

wife claimed any portion of the credit, that portion would be prorated based on the number of months of her Wisconsin residency in 1980. For example, if she claimed the whole exemption credit, the \$20 credit for each spouse would be prorated based on six months residency to arrive at a total credit allowed to her of \$20 ( $\$20 \times .50 = \$10$  for each spouse;  $\$10 + \$10 = \$20$  total credit allowed).

Situation 2: Part-year resident and nonresidentFACTS:

Taxpayer is a single individual and a resident of Wisconsin for three months in 1980 until her marriage to a nonresident of Wisconsin at which time she moves out of Wisconsin. She is a part-year resident of Wisconsin for three months in 1980 and her husband is a nonresident of Wisconsin for the entire year 1980. Husband has two dependents.

Joint federal adjusted gross income (husband and wife)	\$15,000
Wife's Wisconsin total income (1980 Form 1, Line 38)	\$ 5,000
Husband's Wisconsin total income (1980 Form 1, Line 38)	-0-
Total itemized deductions available for Wisconsin	\$ 3,500

SOLUTION:

The first step is to determine whether the itemized deductions or the Wisconsin standard deduction is greater. Using Table C of the part-year residents and nonresidents standard deduction tables, and Wisconsin combined total income of \$5,000, a standard deduction of \$4,000 is determined. There would be no add-on for dependents since their federal adjusted gross income exceeds \$12,000. Therefore, the \$4,000 standard deduction would be prorated since it is larger than the itemized deductions (\$3,500). To prorate this amount, the ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income is used to find the allowable standard deduction of \$1,333 [ $\$4,000 \times (\$5,000 \div \$15,000) = \$1,333$ ]. Since the husband (a nonresident) has no Wisconsin income, he would not claim any personal exemption credit. The exemption credits would be claimed by the wife (a part-year resident) and must be prorated using the part-year resident method. There are four exemptions (husband, wife and two dependents) for a total of \$80 available and these would be prorated based on the number of months (3) that the wife was a resident of Wisconsin in 1980. The total allowable credit would be \$20 ( $\$20 \times .250 = \$5$  for each spouse,  $\$40 \times .250 = \$10$  for dependents;  $\$5 + \$5 + \$10 = \$20$  total credit allowed).

Situation 3: Part-year resident and nonresidentFACTS:

Taxpayer is a widow with four dependents and is a Wisconsin resident for six months in 1980 until her marriage to a nonresident of Wisconsin after which she moves out of Wisconsin. Her spouse has two dependents.

Joint federal adjusted gross income (husband and wife)	\$100,000
Husband's Wisconsin total income (1980 Form 1, line 38)	\$ 5,000
Wife's Wisconsin total income (1980 Form 1, line 38)	\$ 5,000
Total itemized deductions available for Wisconsin	\$ 15,000

**SOLUTION:**

The itemized deductions would require proration using the ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income. The allowable deduction would be \$1,500 [ $\$15,000 \times (\$10,000 \div \$100,000)$ ]. This amount could be divided between spouses in any manner they choose. The manner in which the amount of personal exemption credit available is to be prorated is dependent on which spouse claims the credit. There are eight exemptions (husband, wife and 6 dependents) or \$160 available for prorating. If the wife (a part-year resident) claimed the whole credit, the allowable amount would be \$80 ( $\$20 \times .500 = \$10$  for each spouse,  $\$120 \times .500 = \$60$  for dependents;  $\$10 + \$10 + \$60 = \$80$  total credit allowed). If the husband (a nonresident) claimed the credit, the allowable amount would be \$16 [ $\$20 \times (\$10,000 \div \$100,000) = \$2$  for each spouse,  $\$120 \times (\$10,000 \div \$100,000) = \$12$  for dependents;  $\$2 + \$2 + \$12 = \$16$  total credit allowed]. Therefore, the total personal exemption credit allowed would vary depending on which spouse claimed the credit.

**Situation 4: Part-year resident and nonresident****FACTS:**

Taxpayer is single and a resident of Wisconsin for one month in 1980 until her marriage to a nonresident after which she moves out of Wisconsin. There are no dependents.

Joint federal adjusted gross income (husband and wife)	\$25,000
Husband's Wisconsin total income (1980 Form 1, line 38)	\$ 2,500
Wife's Wisconsin total income (1980 Form 1, line 38)	-0-
Total itemized deductions available for Wisconsin	-0-

**SOLUTION:**

The first step is to determine the correct available deduction. Using Table C of the part-year residents and nonresidents standard deduction tables, a deduction of \$4,000 would be determined. This amount would be prorated using the ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income to get the allowable deduction of \$400 [ $\$4,000 \times (\$2,500 \div \$25,000)$ ]. The total personal exemption credit available for two exemptions is \$40. Since the husband (a nonresident) would be claiming the entire credit (because the part-year resident wife has no income), the allowable amount would be \$4 [ $\$20 \times (\$2,500 \div \$25,000) = \$2$  for each spouse;  $\$2 + \$2 = \$4$  total credit allowed]. Since this is less than the \$5 minimum total personal exemption credit allowable, the \$5 minimum should be claimed.

**Situation 5: Full-year resident and nonresident****FACTS:**

Wife is a full-year resident of Wisconsin for 1980, married to a person who is a nonresident of Wisconsin for the entire year 1980. They maintain separate domiciles for the entire year 1980. Wife has one dependent and husband has one dependent.

Joint federal adjusted gross income (husband and wife)	\$40,000
Wife's Wisconsin total income (1980 Form 1, line 38)	\$ 6,000
Husband's Wisconsin total income (1980 Form 1, line 38)	\$10,000
Total itemized deductions available for Wisconsin	\$ 6,000

**SOLUTION:**

Since wife is a full-year resident of Wisconsin, any deductions or exemption credit claimed by her need no proration. If, for example, she claimed the full \$6,000 of itemized deductions, she is allowed the entire amount. Any amount of itemized deductions claimed by the husband (a nonresident) must be prorated using the ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income. For example, if the wife (a full-year resident) claims \$1,000 of deduction, no proration of that amount would be required. The \$5,000 allocated to the husband would have to be prorated to determine his allowable deduction of \$2,000 [ $\$5,000 \times (\$16,000 \div \$40,000)$ ]. There are four exemptions (husband, wife and 2 dependents) or a total of \$80 available. If the full-year resident wife claimed the entire \$80, no proration would be needed. If the nonresident husband claimed the \$80, his allowable credit would be \$32 [ $\$20 \times (\$16,000 \div \$40,000) = \$8$  for each spouse,  $\$40 \times (\$16,000 \div \$40,000) = \$16$  for dependents;  $\$8 + \$8 + \$16 = \$32$  total credit allowed].

**Situation 6: Full-year resident and nonresident****FACTS:**

Taxpayer is a full-year resident of Wisconsin for 1980 who marries a nonresident on December 31, 1980. Her spouse is a nonresident for the entire year 1980. There are no dependents.

Joint federal adjusted gross income (husband and wife)	\$40,000
Husband's Wisconsin total income (1980 Form 1, line 38)	\$10,000
Wife's Wisconsin total income (1980 Form 1, line 38)	-0-
Total itemized deductions available for Wisconsin	\$ 8,000

**SOLUTION:**

The husband (a nonresident) would be claiming the itemized deductions since the wife had no income. Therefore the itemized deductions must be prorated using the ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income to get \$2,000 allowable [ $\$8,000 \times (\$10,000 \div \$40,000)$ ]. The personal exemption credits would be prorated using the

same formula since the husband would be claiming the credit. A total of \$40 is available, so the prorated credit would be \$10 [ $\$20 \times (\$10,000 \div \$40,000) = \$5$  for each spouse;  $\$5 + \$5 = \$10$  total credit allowed].

#### Situation 7: Both part-year residents but for different periods

##### FACTS:

Taxpayer was a nonresident of Wisconsin who moved into Wisconsin on April 1, 1980 (he was a part-year resident of Wisconsin for 9 months in 1980). He then marries a nonresident who also moves to Wisconsin on October 1 (she was a part-year resident for 3 months in 1980). There are no dependents, but wife is over age 65.

Joint federal adjusted gross income (husband and wife)	\$10,000
Husband's Wisconsin total income (1980 Form 1, line 38)	\$ 5,000
Wife's Wisconsin total income (1980 Form 1, line 38)	\$ 1,000
Total itemized deductions available for Wisconsin	-0-

##### SOLUTION:

Since both husband and wife are part-year residents, the amount of standard deduction available requires proration based on the ratio of the spouses' combined Wisconsin total income to their joint federal adjusted gross income. Using Table D of the part-year residents and nonresidents standard deduction tables, and combined Wisconsin total income of \$6,000, a standard deduction of \$4,800 is determined. The allowable prorated standard deduction would be \$2,880 [ $\$4,800 \times (\$6,000 \div \$10,000)$ ]. This total can be divided between husband and wife in any way they choose. A total personal exemption credit of \$45 is available (\$20 exemption credit for the husband and \$25 credit for the wife). If the husband, a part-year resident for nine months, claims the whole \$45, a total credit of \$33.75 would be allowed ( $\$20 \times .75 = \$15$  for husband,  $\$25 \times .75 = \$18.75$  for wife;  $\$15 + \$18.75 = \$33.75$  total credit allowed). If the wife, a part-year resident for three months, claims the whole \$45, a total of \$11.25 would be claimed by her ( $\$20 \times .25 = \$5$  for husband,  $\$25 \times .25 = \$6.25$  for wife;  $\$5 + \$6.25 = \$11.25$  total credit allowed).

#### CORPORATION INCOME/FRANCHISE TAX

##### I. Corporation's Rental Income and Sale of Rental Property

**Facts & Questions:** A corporation headquartered outside of Wisconsin has a Wisconsin division that manufactures products, has retail sales of its manufactured products, rents its manufactured products and has sales of its rented manufactured products both within and without Wisconsin. The Wisconsin Supreme Court in Kearney & Trecker Corporation vs. Wisconsin Department of Revenue (91 Wis.2d 746, October 9, 1979) stated that income derived from the lease of tangible personal property follows the situs of the property from which derived. How is the rental income from manufactured products to be treated? How are sales of equipment previously rented to be treated?

**Answers:** Rental income from the manufactured products follows the situs of the property and is non-apportionable under s. 71.07 (1m), Wis. Stats. Gains and losses on the disposal of the previously rented property are business income or loss and subject to apportionment for the years 1976 and thereafter.

##### II. Wisconsin Net Operating Loss and Wisconsin Net Operating Loss Carryforward

For income years 1976 and thereafter, s. 71.06, Wis. Stats., provides that a corporation may offset against its Wisconsin net business income any Wisconsin net business loss sustained in any of the next 5 preceding income years to the extent not offset by other items of Wisconsin income in the loss year and by Wisconsin net business income of any year between the loss year and the income year for which an offset is claimed. Income having a Wisconsin situs under s. 71.07 (1m), Wis. Stats., whether taxable or exempt, shall be included in Wisconsin income and Wisconsin net business income. How is s. 71.06 interpreted as it relates to the situations described below:

- What constitutes an income year?  
Any period for which a corporation is required to file a return in an income year. This normally is for a 12 month period. However, if a corporation changes its year end from one fiscal year to another fiscal year or calendar year or from a calendar year to a fiscal year, a short period return is required (in no case shall a return be made for a period of more than 12 months). In such a case, this short period return constitutes one income year.
- What happens to the net business loss of a corporation which is a party to a reorganization?  
If the laws of the state pursuant to which the reorganization was accomplished provide for continued existence of the dissolved company in the survivor, the Wisconsin net business loss may be carried forward; if they do not provide for continued existence, the Wisconsin net business loss may not be carried forward. The laws of Wisconsin do not provide for continued existence, so that in reorganizations accomplished pursuant to Wisconsin statutes, the Wisconsin net business loss of the dissolved corporation cannot be carried forward.
- For what items of income must the loss be adjusted or offset against? The Wisconsin net business loss reported for tax purposes must be adjusted for such items as exempt interest, deductible dividends, and nontaxable life insurance proceeds. The income to which this loss is carried forward must be adjusted for these same items (exempt interest, deductible dividends and nontaxable life insurance proceeds) plus Section 337 capital gains that were excluded from income.
- How Wisconsin net business loss offset is determined.
  - "Wisconsin only" Corporation. A corporation which has business income only attributable to Wisconsin is required to adjust its Wisconsin net business loss offset by the items mentioned in part c. above. If the corporation has other non-business income outside Wisconsin (income following situs of property) pursuant to s. 71.07 (1m), Wis. Stats., it is not required to adjust its loss by this nontaxable income. The fol-